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February 28, 1991

Terry L. Polley, Esq.  
AJALAT & POLLEY  
643 S. Olive Street, Suite 200  
Los Angeles, CA 90014

Dear Mr. Polley:

This is in response to your letter of February 15, 1991 to Richard Ochsner in which you request our opinion as to whether there would be a change in ownership as a result of the following hypothetical facts set forth in your letter.

**Facts**

In 1980, the taxpayer entered into a lease from a public agency whose property is exempt from property taxes. The original term of the lease is ten years, with two five-year options. The possessory interest is appraised in 1980, using twenty years as the reasonably anticipated term. In 1985, the taxpayer adds two additional five-year options with regard to the property. In 1990, the taxpayer exercises its first five-year option.

With respect to the above facts, you ask whether the exercise of the first five-year option in 1990 is a change in ownership requiring the assessor to reappraise the possessory interest at that time.

Revenue and Taxation Code\* section 60 defines "change in ownership" as:

a transfer of a present interest in real property, including the beneficial use thereof, the value of which is substantially equal to the value of the fee interest.

Section 61 provides in relevant part that change in ownership, as defined in section 60 includes:

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\* All statutory references are to the Revenue and Taxation Code unless otherwise indicated.

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. . . .

(b) The creation, renewal, sublease, or assignment of a taxable possessory interest in tax exempt real property for any term. For purposes of this subdivision, "renewal" does not include the granting of an option to renew an existing agreement pursuant to which the term of possession of the existing agreement would, upon exercise of the option, be lengthened, whether the option is granted in the original agreement or subsequent thereto.

It is well established that leasing publicly owned tax exempt real property to a private party creates a taxable possessory interest in the private party and is thus a "change in ownership" for property tax purposes. (§§ 60, 61(b), 107; Host International, Inc. v. County of San Mateo (1973) 35 Cal. App. 3d 286, 289; 18 Cal. Code Regs. §§21, 462(e), 467 (Property Tax Rules).)

Thus, when the taxpayer entered into the lease of real property from the tax exempt public agency in 1980, a taxable possessory interest was created and a change in ownership under section 61(b) occurred. Pursuant to section 61(b), no "renewal" of the possessory interest occurred when the taxpayer was granted two additional five-year options to renew.

With respect to whether a renewal of a possessory interest occurred for purposes of section 61(b) and Property Tax Rules 462(e) and 467 when the first five-year option was exercised in 1990, Property Tax Rule 21 provides:

The following definitions govern the construction of the words in the rules pertaining to possessory interests.

. . . .

(h) "Extended" or "renewed" means the lengthening of the term of possession of an agreement by mutual consent or by the exercise of an option by either party to the agreement.

Since the term of possession of the lease was ten years, such term would have expired in 1990 had an option to renew not been exercised. Accordingly, the exercise of the option in 1990 by the taxpayer lengthened the term of possession granted under the lease and constituted a renewal of the the taxable possessory interest for purposes of sections 61(b) and Property

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Tax Rules 21(h), 462(e) and 467 and was therefore a change in ownership of the taxable possessory interest.

The case of Wrather Port Properties, Ltd. v. Los Angeles County (1989) 209 Cal. App. 3d 517 is distinguishable in our view. In that case, the taxpayer and the city executed a lease of real property in October, 1980, for a term of 40 years, the maximum term then allowed by the city charter. At the time the lease was signed, however, a charter amendment increasing the permissible maximum term to 66 years was on the ballot for an election less than a month later. The lease provided that if the charter amendment passed, the term of the lease "shall be extended" accordingly "and the parties shall promptly execute an amendment to this Lease stating the new expiration date." The voters approved the charter amendment and it took effect in December 1980. In December 1981, the taxpayer and the city executed an amendment to the lease extending the term of possession from 40 to 66 years as required by the lease.

In 1983 the Assessor assessed the possessory interest created by the original lease. In 1985, the Assessor revalued the possessory interest on the grounds that the automatic increase in the term of the lease from 40 to 66 years was a change in ownership. In the ensuing property tax refund action, the trial court found as facts: (1) The taxpayer and the city entered into the lease "based on the reasonable expectation of a maximum 66 year term"; (2) "The original lease specified a term equal to the maximum term allowed by the City Charter; (3) "In making the initial assessment . . . the Assessor was aware of the Lease and First Amendment, recognized the lease was for 66 years and treated it as a change in ownership", the "First Amendment" to the original lease accomplished the mechanical specification of the 66 year term granted in the original lease." Based on these facts, the trial court concluded "[T]he original lease created the rights to a 66 year term and there has been no subsequent change of ownership for the years involved. . .".

The Court of Appeal held that under the facts of this case, the trial court properly concluded that the extension of the lease between the taxpayer and the city did not constitute a change in ownership. Essentially, the court concluded that the amendment to the lease did not lengthen the lease term since under all the facts, the lease term was 66 years under the original lease. Thus, there was no renewal of the possessory interest and hence, no change in ownership.

As indicated above, the hypothetical case is distinguishable in that the exercise of the option in 1990 did lengthen the term

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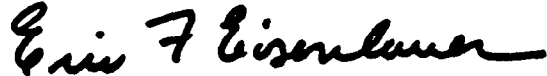
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of the lease which would have expired had the option not been exercised or had the lease not otherwise been extended or renewed.

The views expressed in this letter are advisory only and are not binding upon the assessor of any county. You may wish to consult the the appropriate assessor in order to confirm that the subject property will be assessed in a manner consistent with the conclusion stated above.

Our intention is to provide timely, courteous and helpful responses to inquiries such as yours. Suggestions that help us to accomplish this goal are appreciated.

Very truly yours,



Eric F. Eisenlauer  
Tax Counsel

EFE:ta  
3056D

cc: Mr. John W. Hagerty  
Mr. Verne Walton

## **CHANGE IN OWNERSHIP (Contd.)**

- | 220.0550 **Possessory Interests.** When taxable property is purchased by a tax exempt governmental agency pre-existing leases become taxable as possessory interests, assuming that they satisfy the requirements of Property Tax rule 21. Any renewal, extension, sublease or assignment of such a possessory interest is a change in ownership, regardless of the term of possession remaining under the lease; whereas transfers of leasehold interests in taxable property constitute changes in ownership depending on the terms of possession remaining as provided in Revenue and Taxation Code section 61(c)(1) and (2). C 8/9/91.